GA1.13:GGD-81-13/SUM.

JAN 2 1981

BY THE COMPTROLLER GENERAL

ORIGINAL

Report To The Congress

OF THE UNITED STATES

Examinations Of Financial Institutions Do Not Assure Compliance With Consumer Credit Laws

Financial regulatory agencies' programs for enforcing consumer credit protection laws were inconsistent and, for the substantive aspects of some laws, inadequate. As a result, consumers have not been assured consistent protection, and financial institutions have not been treated equally.

GAO recommends that regulators modify their programs to emphasize the substantive principles of consumer credit laws. Regulators should reassess the objectives of compliance examinations, continue plans to recruit and train specialized examiners, adopt uniform detailed examination procedures, and establish uniform standards for enforcing compliance with consumer credit laws.

GGD-81-13
JANUARY 2, 1981

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COMPTROLLER GENERAL'S REPORT TO THE CONGRESS

EXAMINATIONS OF FINANCIAL INSTITUTIONS DO NOT ASSURE COMPLIANCE WITH CONSUMER CREDIT LAWS

D I G E S T

Consumer credit protection laws set forth basic principles to protect and inform consumers seeking credit. These principles include:

--Equal opportunity to obtain credit, free of discrimination by sex, race, color, religion, age, national origin, or marital status.

--Meaningful disclosure of terms and conditions of credit.

--Fair reporting and use of personal credit information.

--Fair debt collection practices.

--Reasonable efforts by financial institutions to help meet the credit needs of their local communities.

Financial institutions are responsible for complying with these laws. Financial institution regulators--the Federal Deposit Insurance Corporation, Federal Home Loan Bank System, Federal Reserve System, National Credit Union Administration, and Office of the Comptroller of the Currency--supervise institutions that extend credit such as banks, savings and loan associations, and credit unions. The regulators have responsibilities for ensuring that financial institutions comply with the laws so that consumers are afforded the protection provided by the laws.

GAO found that the agencies' programs for identifying violations and enforcing compliance with the laws were inconsistent and, for the substantive aspects of some laws, inadequate. As a result, consumers

have not been assured consistent protection, and financial institutions have not been treated equally.

By focusing on technical compliance with only limited attention to substantive matters, regulators have fueled a long-standing controversy over consumer protection laws. Opponents of such laws say their costly requirements do not address the principles of the laws, while proponents contend that the basic requirements of the laws are not being enforced by regulatory agencies.

INCONSISTENT AND INADEQUATE COMPLIANCE EXAMINATIONS

Agencies were not consistently or adequately examining financial institutions' compliance with some consumer credit protection laws. For the most part, agencies identified violations of technical requirements involving forms and disclosures, whereas violations of the substantive principles of some laws, such as discriminatory practices, were seldom cited. Agencies were also inconsistent in the laws chosen for compliance examination, the amount of effort expended on examinations, and the types and quality of analyses made during examinations.

In examining for compliance with consumer laws, agencies generally reviewed the stated policies of an institution, the forms it used, and how well it met the technical requirements of the laws. This approach was inadequate to validate compliance with the substantive principles of some consumer laws. For example, GAO found that the approach normally enabled agencies to adequately assess compliance with the principle of meaningful disclosure of terms and conditions of credit as required by the Truth in Lending Act. On the other hand, the approach hindered agencies in assessing compliance with such principles as equal credit opportunity and institutions' efforts to help meet local community credit needs.

Examinations for compliance with these requirements were generally inadequate.

Examiners performed few specific analyses to test institutions' practices (such as comparing accepted versus rejected loans) and generally only reviewed institutions' forms and talked to institutions' management.

Consumers not assured protection of the law

The inconsistencies in agencies' examination programs resulted in differences in the number and type of violations identified. Assuming the identification of violations effects a change in an institution's policies, these differences ultimately affect the protection afforded to individuals seeking credit.

Weaknesses in agencies' methods of examining for compliance, particularly with regard to compliance with equal credit opportunity principles, prevent the agencies from identifying violations which should be corrected to assure consumers they will be treated in accordance with the law when seeking credit at a financial institution.

AGENCIES NEED UNIFORM COMPLIANCE ENFORCEMENT STANDARDS

The enforcement of compliance with consumer laws varies by agency and by region within an agency. Agencies were generally not effective in obtaining compliance from institutions which did not voluntarily respond to verbal and written requests for corrective action.

GAO's sample of violations reported for 110 institutions showed that financial institutions voluntarily acted to correct violations brought to their attention by Federal regulators about 77 percent of the time. However, for 23 percent of the violations, institutions did not take corrective actions and the agencies generally

did not take additional steps to enforce compliance. About one half of the institutions in GAO's sample continued to violate at least one provision of the laws from one examination to the next. Agencies' enforcement actions generally did not become progressively stronger, and they rarely used a cease and desist order to obtain corrective action.

GAO recognizes that since 1977 the agencies have made substantial progress in correcting these shortcomings, and momentum for improvement continues. Uniform guidelines have been adopted to examine for and enforce compliance with some laws. More changes are needed, however, if the agencies are to achieve the level of supervision needed to assure consumers the protection provided for in the laws. A task force to assess consumer examination was recently established by the Comptroller of the Currency. GAO believes the task force's goals provide an excellent framework for all of the agencies to consider needed changes.

RECOMMENDATIONS

The Chairmen of the Federal Deposit Insurance Corporation, Federal Home Loan Bank Board, Federal Reserve Board, and National Credit Union Administration and the Comptroller of the Currency should work together, under the direction of the Federal Financial Institutions Examination Council, to develop and administer consistent, effective consumer law compliance examination programs that adequately address the substantive principles of the laws. Specifically, the agencies should:

--Reassess the nature and objectives of compliance examinations.

--Place greater training emphasis on examination techniques that assess substantive principles of the laws and regulations.

--Develop uniform examination procedures for all consumer protection laws to effectively assess compliance with the substantive as well as the technical provisions of consumer laws.

--Determine and allocate the level of resources necessary to effectively implement uniform examination procedures.

--In the case of the Federal Home Loan Bank System, establish separate career paths for consumer law compliance examiners.

The Federal Financial Institutions Examination Council should monitor the progress of the Comptroller of the Currency's task force on consumer examination to determine the applicability and value of such a review for the other financial institution regulatory agencies.

The agencies should establish uniform standards for enforcing compliance with consumer laws, recognizing the varying significance of violations, and stating clearly the penalties that will be applied consistently for noncompliance. These standards should be transmitted to the financial institutions.

AGENCY COMMENTS

The agencies and the Examination Council generally agreed with GAO's recommendations. Since the completion of the review, the agencies, individually and under the direction of the Examination Council, have initiated several actions to improve their examination programs and to establish uniform enforcement standards.

Specific agency comments are incorporated as appropriate throughout the report and presented in total in appendices III through VIII.

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ABBREVIATIONS

CRA	Community Reinvestment Act
ECOA	Equal Credit Opportunity Act
FDIC	Federal Deposit Insurance Corporation
FHA	Fair Housing Act
FHLBS	Federal Home Loan Bank System
FRS	Federal Reserve System
HMDA	Home Mortgage Disclosure Act
NCUA	National Credit Union Administration
OCC	Office of the Comptroller of the Currency
TIL	Truth in Lending